

**Supporting Statement for
Semiannual Report of Derivatives Activity
(FR 2436; OMB No. 7100-0286)**

Summary

The Board of Governors of the Federal Reserve System, under delegated authority from the Office of Management and Budget, proposes to extend for three years, without revision, the Semiannual Report of Derivatives Activity (FR 2436; OMB No. 7100-0286). This voluntary report collects derivatives market statistics from seven large U.S. dealers of over-the-counter (OTC) derivatives. Data are collected on notional amounts and gross market values of the volumes outstanding of broad categories of foreign exchange, interest rate, equity- and commodity-linked over-the-counter derivatives contracts across a range of underlying currencies, interest rates, and equity markets. The estimated annual burden for this report is 1,400 hours.

This collection of information complements the ongoing triennial Survey of Foreign Exchange and Derivatives Market Activity (FR 3036; OMB No. 7100-0285). The FR 2436 collects similar data on the outstanding volume of derivatives, but not on derivatives turnover. As with the FR 3036, the Federal Reserve conducts this report in coordination with other central banks and forwards the aggregated data furnished by U.S. reporters to the Bank for International Settlements (BIS), which publishes global market statistics that are aggregations of national data.

Although no changes are proposed to the FR 2436 at this time, if the G-10 central banks determine that additional data should be collected semiannually, then the Federal Reserve would propose revisions to the FR 2436 to include such additional data. The Federal Reserve intends to use data from the FR 3036, as well as the aggregate data reported to the BIS from other reporting countries for the triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity, to determine (in consultation with other reporting countries) whether additional information should be collected on the FR 2436. In addition, the G-10 central banks are currently planning to collect semiannual data on credit default swaps. When the scope of such data is agreed upon by the G-10 central banks, there may be proposed revisions to the FR 2436 in early 2004 to include data on credit default swaps.

Background and Justification

In January 1997, the Governors of the Central Banks of the Group of Ten Countries (G-10) approved a proposal by the Euro-currency Standing Committee (now called the Committee on the Global Financial System) to collect data on global derivatives activity from leading dealers, beginning at the end of June 1998. The Yoshikuni group, a working group of the Euro-currency Standing Committee, developed the reporting framework in a July 1996 report. The report outlined the derivatives market statistics that would be useful to central banks for oversight of global financial markets. They based the report design on the Common Minimum Framework that was developed and released jointly by the Basle Committee on Banking Supervision and the Technical Committee of the International Organization of Securities Commissions (IOSCO) in May 1995. The report also outlined the methodological considerations for collecting and aggregating

gating these data. For example, the working group developed techniques to avoid double counting in the calculation of global market size statistics and fleshed out the level of detail required in data collection efforts.

The report design draws on the results of the April 1995 triennial Central Bank Survey of Foreign Exchange and Derivatives Activity. This survey was the first major coordinated effort by the G-10 central banks to collect data on global derivatives activity. The semiannual FR 2436 was designed to complement the triennial FR 3036 using the same format for reporting derivatives positions outstanding on both reports. This procedure avoids duplication of effort for institutions participating in both data collections and improves the comparability of the data collected by the two reports. Furthermore, the Federal Reserve uses the FR 3036 data to monitor the growth of the derivatives activities at dealers not participating in the FR 2436 panel and to update the FR 2436 panel as necessary to maintain coverage of the vast majority of global derivatives activities.

The purpose of the FR 2436 is to obtain comprehensive and internationally consistent information on the size and structure of the OTC derivatives markets. The statistics are useful to the Federal Reserve, other central banks, and other parties who monitor patterns of activity in financial transactions. Due to the global nature of derivatives activity, only the cooperative efforts of central banks can generate the statistics required for effective monitoring of this activity. The Federal Reserve's involvement in this international reporting program, therefore, is necessary to ensure the availability of statistics necessary for oversight of international financial markets. The FR 2436 provides comprehensive and consistent measures of global derivatives market size and participation not currently available from other sources.

Description of Information Collection

The panel of derivatives dealers provides data on outstanding positions (notional, gross positive and gross negative market values) with breakdowns by market risk category, product type, counterparty type, maturity, and underlying currency or equity market. As well, they provide data on the gross market value of the entire portfolio, before and after netting.

Notional amounts outstanding. A sum of notional amounts outstanding provides a means of approximating the scale and character of market transactions, in much the same manner as a sum of principal amounts provides for the cash market. Allocating notional amounts outstanding to market risk, currency, instrument, maturity, and counterparty categories provides greater insight into the exposures to price risks transferred between contracting parties. Additionally, regularly published data on notional amounts enhance market transparency and permit market participants to compare, over time, the size and composition of their derivatives activities with those taking place in the market as a whole.

Gross positive and negative market values. Gross market value figures show the magnitude of unsettled changes in value of derivatives contracts outstanding at the time of reporting. Semiannual reporting produces a series of changes in gross market value over time. Such a time series is a valuable source of information for researchers and market participants in

developing an understanding of the role and function of derivatives markets in financial systems in various circumstances.

The 1995 global survey of derivatives markets found small net market value positions in derivatives for reporting U.S. dealers. The average net market value as a percentage of the total market value for foreign exchange and interest rate derivatives contracts with customers, foreign dealers, and non-reporting dealers was 1 percent. These positions were interpreted as showing that derivatives dealers had not taken large net exposures in meeting customer demands in derivatives. The availability of a time series of semiannual data on market values provides a means to better assess the risk intermediation services that are being offered by dealers as a group.

Furthermore, gross market values can be used as one measure of market size; they show, at a given point in time, the amount of risk that is transferred using derivatives contracts. Although, this measure requires summing the gross positive market values of *all* market participants (not just of reporters), the gross positive market value of non-reporting firms can be captured by measuring the negative market value of reporting firms' contracts with non-reporting firms. Thus, market size statistics based on gross market value can be constructed while maintaining a limited reporting population.

As indicated, the outstandings data collected on the FR 2436 are disaggregated several ways.

Market risk categories: foreign exchange and gold derivatives, single-currency interest rate derivatives, and equity-linked and commodity derivatives

Product types: forward contracts, swaps, and bought and sold OTC options

Counterparty types: reporting dealers, non-reporting financial institutions, and other institutions

Maturities: one year or less, over one year through five years, and over five years

Currency or equity market: Data for foreign exchange and single-currency interest rate contracts are reported by currency for each G-10 currency, as well as for any additional currency for which a material amount of contracts is outstanding. Data on equity-linked derivatives are reported in the six categories: U.S., Japanese, European (excluding emerging markets in eastern Europe), Latin American, Other Asian, and Other.

Reporting Panel

The reporting panel, together with reporters from other reporting countries, represents approximately 90 percent of total global activity in each of the major categories of derivatives. Firms were selected as potential reporters based on the size of their derivatives positions reported in the April 1995 triennial derivatives market survey. Subsequent triennial surveys have shown that expansion of the reporting panel is not necessary. Seven U.S. institutions participate in the

current reporting panel: BankAmerica, Bank One, Citigroup, Goldman Sachs, JP Morgan Chase, Merrill Lynch, and Morgan Stanley Dean Witter.

The Federal Reserve would solicit new respondents to the FR 2436 reporting panel from those that report significant data as of June 30, 2004, on the derivatives outstanding portion of the FR 3036 survey. The FR 3036 reporting panel includes U.S. banking institutions that have \$1 billion or more in foreign exchange and interest rate contracts reported on their Consolidated Financial Statements for Bank Holding Companies (FR Y-9C; OMB No: 7100-0128), as well as banks and nonbanks identified through commercial trade directories and from the reporting panels of the Treasury Foreign Currency reporting system.

Frequency

Respondents file the FR 2436 semiannually, as of the close of business each June 30 and December 31. Although the proposal implementing this information collection anticipated a possible change to quarterly reporting in 2000, the G-10 central banks have not yet determined that the burden of more frequent reporting is justified.

Possible Future Revisions

The G-10 central banks are planning to collect semiannual data on credit default swaps. They have agreed upon the reporting template but have yet to work out reporting instructions. Therefore, proposed revisions to the FR 2436 are likely to be submitted through the Federal Reserve's reports clearance process in early 2004, with an effective date of mid- or end-2004.

As a general rule, the Federal Reserve intends to use FR 3036 data from April 2004 to determine whether additional information should be collected on the FR 2436. With this approach, reporters would not have to change their internal data collection systems for the FR 2436 until the significance of possible new items is determined. If possible new items are collected on the FR 3036 and prove to be significant, then the Federal Reserve would propose to add the items to the semiannual FR 2436. For this reason, on an ongoing basis, it may be desirable to renew the FR 2436 shortly after receipt of data from the triennial FR 3036 to accommodate such possible revisions.

Time Schedule for Information Collection and Publication

Data are submitted to the Federal Reserve Bank of New York within sixty days of the as-of dates, June 30 and December 31 each year. After editing the data, Federal Reserve Bank of New York sends the aggregated data to the BIS and to the Board. The BIS compiles the data from reporting U.S. institutions with those from the approximately seventy additional reporters from other G-10 countries and constructs and publishes global derivatives market statistics. The Securities and Exchange Commission receives copies of the reports from the reporting securities firms.

When the G-10 central banks approved this information collection, they anticipated that the due date could be shortened to one month. The G-10 central banks believe at this time it would be too burdensome to ask reporters to file in less than sixty days. However, the G-10 central banks would still like to change the reporting due date to thirty days at some time in the future.

Legal Status

The Board's Legal Division has determined that this report is authorized by law [12 U.S.C. §§ 248(a), 353-359, and 461] and is voluntary. Individual respondent data are regarded as confidential under the Freedom of Information Act [5 U.S.C. §552(b)(4)].

Consultation Outside the Agency

There has been no outside consultation.

Estimate of Respondent Burden

As shown in the table below, the annual reporting burden for this report is estimated to be 1,400 hours. This represents less than 1 percent of total Federal Reserve burden for all reports.

<i>Number of respondents</i>	<i>Annual frequency</i>	<i>Estimated average hours per response</i>	<i>Estimated annual burden hours</i>
7	2	100	1,400

Based on an hourly cost of \$20, the annual cost to the public is estimated to be \$28,000.

Sensitive Questions

This collection of information contains no questions of a sensitive nature, as defined by OMB guidelines.

Estimate of Cost to the Federal Reserve System

The cost of collecting and processing the data falls entirely on the International Reports Division of the FRBNY. The FRBNY's current costs associated with the FR 2436 are estimated at \$100,000 per year.